

RETIREE HEALTH VEBAs

Presentation to Massachusetts OPEB Commission

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Voluntary Employees' Beneficiary Association (VEBA) Trust

- Voluntary Employees' Beneficiary Associations are trusts authorized under IRC § 501(c)(9) that allow employers to make tax-deductible contributions to a trust to fund health care benefits or certain other types of employee benefits
- The VEBA trust is then coupled with an *ERISA-governed* employee welfare benefit plan
 - ERISA requirements make VEBAs less attractive to public sector employers
- VEBAs are the tax structure for the following types of arrangements:
 - Single employer collectively-bargained trusts
 - Taft-Hartley trusts
 - Retiree trusts



Retiree VEBA

- Controlled by trustees appointed by the membership who are independent of the employer
- Trustee Committee has sole and exclusive authority to administer and operate the trust in accordance with the rules set forth in the trust agreement
- Employer can create the trust but does not retain administrative duties or control over assets or trust management
- Funded by the employer at rates bargained
- Assets cannot revert to the employer

Impact on Financial Reporting

Depends on the structure and funding of the VEBA. May count as assets under GASB 45.

Plan Design

- ☑ Defined Contribution or Defined Benefit health plan
- ☑ Determine general eligibility requirements
- ☑ Determine age/service requirements for eligibility for full allowance and for reduced allowance
- ☑ Accrue contribution allowance under unit benefit formula (e.g., \$X or X% for each year of service)
- ☑ Decide on type of benefits

Retiree VEBA Press

Retirees taking over retiree health obligations from their employers:

- UAW/Big 3
- Goodyear
- Navistar
- ALPA/FedEx
- Republic Steel

Primarily defined benefit plans, managed by independent Board of Trustees, paid for by employer through collective bargaining, settlement, or bankruptcy.



Benefits Payable Through a Retiree VEBA

Defined Benefit Plans (some or all)

➤ Medical

- Including Medicare supplements or Medicare Advantage plans

➤ Prescription Drugs

- Including Medicare Part D Plans/EGWPs

➤ Dental

➤ Vision

➤ Life insurance

In Massachusetts, OPEB trusts already exist for prefunding of defined benefit retiree health plans, without the legal issues associated with VEBAs.

Benefits Payable Through a Retiree VEBA

Defined Contribution Plans

- Use VEBA to fund Health Reimbursement Arrangement
 - Fund account over employee's career, so money will be available at retirement.
 - Flexibility in establishing contribution formulas, rollover rules, etc.
- Provide fixed-dollar subsidies, so retirees can purchase benefits on their own
 - Individual Medicare plans
 - Pre-65 retirees could purchase through ACA State Health Exchanges
- Provide supplemental benefits or buydowns
 - Lower required premium contributions
 - Lower deductibles, copays
 - Dental or Vision only

Basic VEBA Requirements

A VEBA must meet the following requirements:

- Must be an employee association
- Membership in the association must be voluntary
- Purpose is to pay life, sickness, accident, or other permissible benefits to its members and dependents
- No part of the net earnings of the organization may inure to the benefit of the employer, private shareholder, or individual

Tax Treatment of VEBA's

- The accident and health coverage provided under a VEBA is excluded from the gross income of employees (including retirees)
- Reimbursement of qualified medical expenses is tax-exempt to employees (including retirees)
 - “Qualified Medical Expenses” as defined by IRC Section 213
- For employers with tax liability, employer contributions to the VEBA are deductible, subject to tax code rules

VEBA Membership

- Organization must be formed on behalf of employees who associate together to receive the benefits provided by the organization
- Employees must share an employment-related common bond
- VEBA meets employee organization standard if 90% of membership are employees, former employees, etc. and their dependents

CAUTION: Non-employees cannot be more than 10% of population. If the VEBA is a Taft-Hartley plan, the MEWA rules require that 85% of the population be collectively bargained



VEBA Earnings

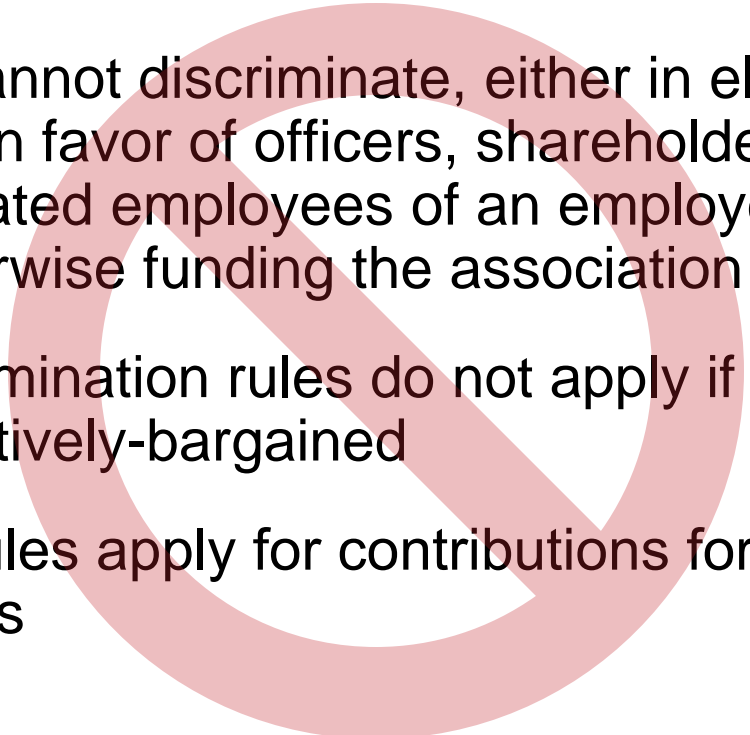
- In general, the earnings on reserves held in a VEBA for future retiree health coverage are taxable (to the extent they exceed the general reserve limit, i.e., IBNR plus administrative cost)
- However, reserves held under collectively bargained plans or employee-pay-all plans are tax exempt
- VEBA funds generally earn tax-free investment income and can be used either to pay benefit claims or insurance premiums. However, VEBAs are subject to unrelated business taxable income (UBTI) tax under tax code §512

Governance



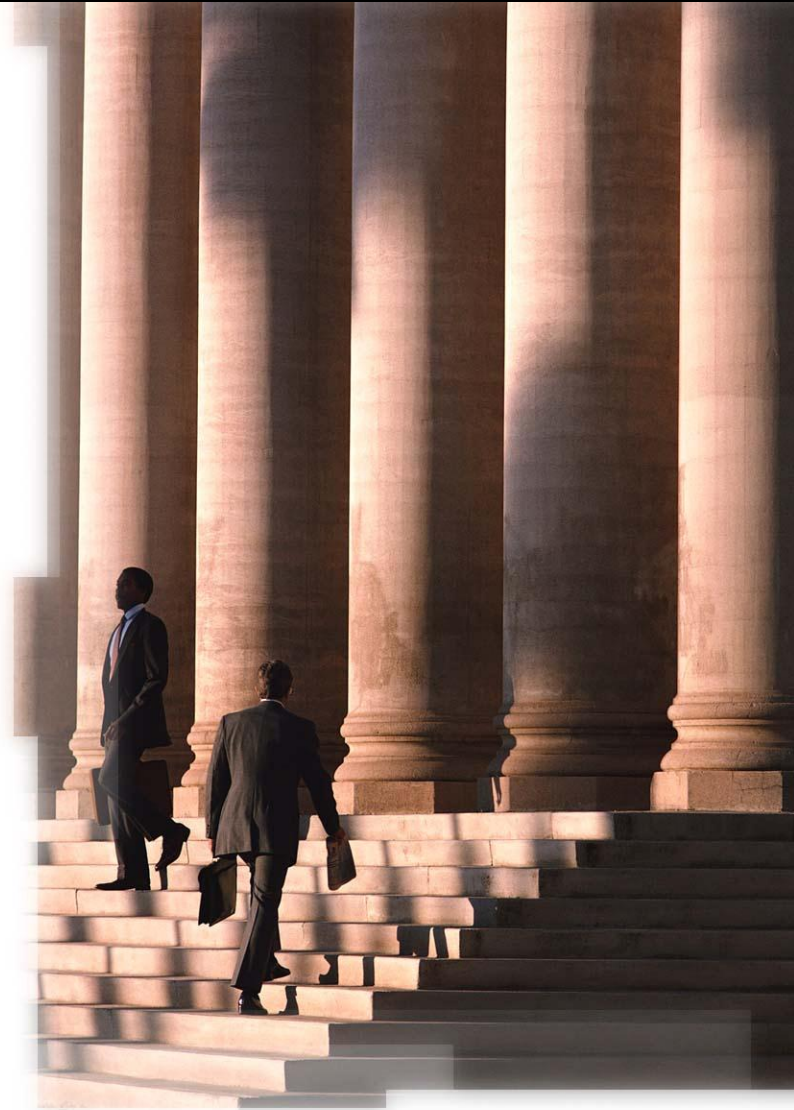
- VEBA must be controlled by the employee membership, an independent trustee(s) or trustees or other fiduciaries at least some of whom are designated on behalf of the employee members

Nondiscrimination rules

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- VEBAs cannot discriminate, either in eligibility or in benefits, in favor of officers, shareholders, or highly compensated employees of an employer contributing to or otherwise funding the association
 - Nondiscrimination rules do not apply if the employees are collectively-bargained
 - Special rules apply for contributions for “key” employees

Operations

- VEBAs must apply to the IRS for a letter that recognizes the tax-exempt status of the trust
- Plan is subject to ERISA's reporting and disclosure, fiduciary, and other requirements



Sample Retiree VEBAs

Committee made of:

- Retirees from employer
- Union appointed members including union officials
- Public/Professionals



Organization Issues

Outline

➤ **Retain Advisors**

➤ **Service Providers**

- Plan Administrator
- Claims Administrator
- Pharmacy Benefit Manager
- Custodial Bank
- Investment Manager(s)

➤ **Documents**

- Trust, Plan and SPD
- Retiree Communications
- Contracts
- Investment Guidelines

➤ **Filing and Disclosures**

➤ **Fiduciary and Fidelity Insurance**

➤ **Policies and Procedures**

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